SIMULATIONS PLUS INC
Form 10-Q
July 15, 2009

SECURITIES AND EXCHANGE COMMISSION
Washington, DC 20549

FORM 10-Q

[X] Quarterly Report Pursuant to Section 13 or 15(d) of the Security Exchange Act of 1934 for the quarterly period ended May 31, 2009

[_] Transmission Report Pursuant to Section 13 or 15(d) of the Security Exchange Act of 1937 for the transition period from _____ to _____

Commission file number: 001-32046

Simulations Plus, Inc.
(Name of registrant as specified in its charter)

California	95-4595609
(State or other jurisdiction of Incorporation or Organization)	(I.R.S. Employer identification No.)

42505 10th Street West
Lancaster, CA 93534-7059
(Address of principal executive offices including zip code)

(661) 723-7723
(Issuer's telephone number, including area code)

Indicate by check mark whether the registrant (1) filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the past 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes [X] No [_]

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer," and "smaller reporting company" in Rule 12b-2 of the Exchange Act.
Large accelerated filer [_] Non-accelerated filer [_] Smaller reporting company [X]

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes [_] No [X]

The number of shares outstanding of the Issuer's common stock, par value $0.001 per share, as of July 10, 2009, was 15,853,089.

Simulations Plus, Inc.
FORM 10-Q
For the Quarterly Period Ended May 31, 2009

Table of Contents

PART I. FINANCIAL INFORMATION

Item 1.	Financial Statements (Unaudited)	Page
	Consolidated Balance Sheets at May 31, 2009 (unaudited) and August 31, 2008 (audited)	2
	Consolidated Statements of Operations for the three months and nine months ended May 31, 2009 and 2008 (unaudited)	3
	Consolidated Statements of Cash Flows for the nine months ended May 31, 2009 and 2008 (unaudited)	4
	Notes to Consolidated Financial Statements (unaudited)	5
Item 2.	Management's Discussion and Analysis or Plan of Operations	
	General	15
	Results of Operations	20
	Liquidity and Capital Resources	24
Item 3.	Quantitative and Qualitative Disclosures about Market Risk	24
Item 4.	Controls and Procedures	24
	PART II. OTHER INFORMATION	
Item 1.	Legal Proceedings	26
Item 2.	Changes in Securities	26
Item 3.	Defaults upon Senior Securities	26
Item 4.	Submission of Matters to a Vote of Security Holders	26
Item 5.	Other Information	26
Item 6.	Exhibits and Reports on Form 8-K	26
Signature		27
	Exhibit – Certifications	

i

Simulations Plus, Inc.

Consolidated Balance Sheets
at May 31, 2009 (unaudited) and August 31, 2008 (audited)

ASSETS

Current assets	May 31, 2009 (unaudited)	August 31, 2008 (audited)
Cash and cash equivalents	$ 7,372,614	$ 5,889,601
Accounts receivable, net of allowance for doubtful accounts and estimated contractual discounts of $437,124 and $319,609	2,649,333	2,105,074
Inventory	375,389	342,051
Prepaid expenses and other current assets	84,930	195,330
Deferred income taxes	300,200	318,400
Total current assets	10,782,466	8,850,456
Investment (note 8)	-	750,000
Capitalized computer software development costs, net of accumulated amortization of $3,705,718 and $3,324,328	1,897,693	1,788,756
Property and equipment, net (note 3)	48,722	102,633
Customer relationships, net of accumulated amortization of $100,364 and $85,029	27,678	43,013
Other assets	18,445	18,445
Total assets	$ 12,775,004	$ 11,553,303

LIABILITIES AND SHAREHOLDERS' EQUITY

Current liabilities		
Accounts payable	$ 265,580	$ 181,230
Accrued payroll and other expenses	525,853	537,363
Accrued bonuses to officer	60,000	60,000
Accrued warranty and service costs	40,199	33,899
Accrued income tax	115,689	-
Deferred revenue	42,333	83,333
Total current liabilities	1,049,654	895,825
Long-Term liabilities		
Deferred income taxes	789,300	742,400
Total liabilities	1,838,954	1,638,225
Commitments and contingencies (note 4)		
Shareholders' equity (note 5)		
Preferred stock, $0.001 par value 10,000,000 shares authorized no shares issued and outstanding	-	-
Common stock, $0.001 par value 50,000,000 shares authorized 16,023,920 and 16,297,400 shares issued and outstanding	4,495	4,769

Additional paid-in capital	6,100,504	6,328,185
Retained Earnings	4,831,051	3,582,124
Total shareholders' equity	10,936,050	9,915,078
Total liabilities and shareholders' equity	$ 12,775,004	$ 11,553,303

Simulations Plus, Inc.

Consolidated Statements of Operations

For the Three Months and Nine Months Ended May 31, 2009 and 2008 (unaudited)

	Three months ended May 31,		Nine months ended May 31,	
	2009 (unaudited)	2008	2009 (unaudited)	2008
Net sales	$ 2,713,524	$ 2,968,353	$ 7,303,536	$ 7,131,837
Cost of sales	543,087	623,756	1,622,456	1,565,209
Gross profit	2,170,437	2,344,597	5,681,080	5,566,628
Operating expenses				
Selling, general, and administrative	989,165	941,982	2,929,578	2,704,765
Research and development	334,151	222,241	995,832	700,086
Total operating expenses	1,323,316	1,164,223	3,925,410	3,404,851
Income from operations	847,121	1,180,374	1,755,670	2,161,777
Other income (expense)				
Interest income	20,105	54,492	73,098	146,715
Miscellaneous income	514	10	557	35
Gain on currency exchange	20,233	11,098	70,449	44,658
Unrealized loss on investment	-	(57,925)	-	(57,925)
Interest expense	-	(67)	-	(67)
Total other income (expense)	40,852	7,608	144,104	133,416
Income before income taxes	887,973	1,187,982	1,899,774	2,295,193
Provision for income taxes	(318,840)	(435,321)	(650,846)	(734,462)
Net income	$ 569,133	$ 752,661	$ 1,248,928	$ 1,560,731
Basic earnings per share	$ 0.04	$ 0.05	$ 0.08	$ 0.10
Diluted earnings per share	$ 0.03	$ 0.04	$ 0.07	$ 0.09
Weighted-average common shares outstanding				
Basic	16,051,133	16,228,900	16,222,867	16,090,239
Diluted	16,925,581	17,868,750	17,194,349	18,266,766

3

Simulations Plus, Inc.

Consolidated Statements of Cash Flows
for the Nine Months Ended May 31, 2009 and 2008 (unaudited)

	Nine months ended May 31,	
	2009	2008
Cash flows from operating activities	(unaudited)	(unaudited)
Net income	$1,248,928	$1,560,731
Adjustments to reconcile net income to net cash provided by operating activities		
Depreciation and amortization of property and equipment	16,609	40,460
Amortization of customer relationships	15,335	19,823
Amortization of capitalized computer software development costs	381,390	334,509
Bad debts	219,998	62,947
Stock-based compensation	129,660	52,540
Deferred income taxes	65,100	567,400
(Increase) decrease in		
Accounts receivable	(764,258)	(816,044)
Inventory	38,741	(29,314)
Other assets	110,400	(47,088)
Increase (decrease) in		
Accounts payable	84,350	68,478
Accrued payroll and other expenses	(11,510)	1,666
Accrued bonuses to officers	-	(141,289)
Accrued income taxes	115,689	11,453
Accrued warranty and service costs	6,300	(6,103)
Deferred revenue	(41,000)	3,200
Net cash provided by operating activities	1,615,732	1,683,369
Cash flows from investing activities		
Purchases of property and equipment	(34,777)	(67,775)
Proceeds from sale of assets	-	16,011
Proceeds from sale of investments	750,000	-
Capitalized computer software development costs	(490,327)	(594,967)
Net cash provided by (used in) investing activities	224,896	(646,731)
Cash flows from financing activities		
Repurchase of common stock	(447,825)	-
Proceeds from the exercise of stock options	90,210	411,677
Net cash provided by (used in) financing activities	(357,615)	411,677
Net increase in cash and cash equivalents	$1,483,013	$1,448,315

Cash and cash equivalents, beginning of year	5,889,601	4,537,714
Cash and cash equivalents, end of period	$7,372,614	$5,986,029
Supplemental disclosures of cash flow information		
Interest paid	$ -	$ 67
Income taxes paid	$ 377,216	$ 180,000

Simulations Plus, Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

Note 1: GENERAL

This report on Form 10-Q for the quarter ended May 31, 2009, should be read in conjunction with the Company's annual report on Form 10-KSB for the year ended August 31, 2008, filed with the SEC on November 26, 2008. As contemplated by the Securities and Exchange Commission under Article 10 of Regulation S-X, the accompanying financial statements and footnotes have been condensed and therefore do not contain all disclosures required by generally accepted accounting principles. The interim financial data are unaudited; however, in the opinion of Simulations Plus, Inc. ("we", "our", "us"), the interim data includes all adjustments, consisting only of normal recurring adjustments, necessary for a fair statement of the results for the interim periods. Results for interim periods are not necessarily indicative of those to be expected for the full year.

Note 2: SIGNIFICANT ACCOUNTING POLICIES

Estimates
Our consolidated financial statements and accompanying notes are prepared in accordance with accounting principles generally accepted in the United States of America. Preparing financial statements requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenue, and expenses. These estimates and assumptions are affected by management’s application of accounting policies. Actual results could differ from those estimates. Significant accounting policies for us include revenue recognition, accounting for capitalized computer software development costs, and accounting for income taxes.

Principles of Consolidation
The consolidated financial statements include the accounts of Simulations Plus, Inc. and its wholly owned subsidiary, Words+, Inc. All significant intercompany accounts and transactions are eliminated in consolidation.

Revenue Recognition
The Company recognizes revenues related to software licenses and software maintenance in accordance with the American Institute of Certified Public Accountants ("AICPA") Statements of Position (SOP) No. 97-2, "Software Revenue Recognition." Software products revenue is recorded when the following conditions are met: 1) evidence of an arrangement exists, 2) delivery has been made, 3) the amount is fixed, and 4) collectability is probable. Post-contract customer support ("PCS") obligations are insignificant; therefore, revenue for PCS is recognized at the same time as the licensing fee, and the costs of providing such support services are accrued and amortized over the obligation period. For Words+ products, the revenue is recorded at the time of shipment, net of estimated allowances and returns.

As a byproduct of ongoing improvements and upgrades for the new programs and new modules of software, some modifications are provided to customers who have already purchased software at no additional charge. Other software modifications result in new, additional cost modules that expand the functionality of the software. These are licensed separately. We consider the modifications that are provided without charge to be minimal, as they do not significantly change the basic functionality or utility of the software, but rather add convenience, such as being able to plot some additional variable on a graph in addition to the numerous variables that had been available before, or adding some additional calculations to supplement the information provided from running the software. Such software modifications for any single product have typically occurred once or twice per year, sometimes more, sometimes less. Thus, they are infrequent. The Company provides, for a fee, additional training and service calls to its customers and

recognizes revenue at the time the training or service call is provided.

Generally, we enter into one-year license agreements with customers for the use of our pharmaceutical software products. We recognize revenue on these contracts when all the criteria under SOP 97-2 are met.

Most license agreements have a term of one year; however, from time to time, we enter into multi-year license agreements. We generally unlock and invoice software one year at a time for multi-year licenses. Therefore, revenue is recognized one year at a time.

Cash and Cash Equivalents
For purposes of the statements of cash flows, we consider all highly liquid investments purchased with original maturities of three months or less to be cash equivalents.

Accounts Receivable
We maintain an allowance for doubtful accounts for estimated losses that may arise if any of our customers are unable to make required payments. We specifically analyze the age of customer balances, historical bad debt experience, customer credit-worthiness, and changes in customer payment terms when making estimates of the collectability of our trade accounts receivable balances. If we determine that the financial conditions of any of our customers deteriorated, whether due to customer-specific or general economic issues, an increase in the allowance may be made. Accounts receivable are written off when all collection attempts have failed.

Inventory
Inventory is stated at the lower of cost (first-in, first-out basis) or market and consists primarily of computers and peripheral computer equipment.

Capitalized Computer Software Development Costs
Software development costs are capitalized in accordance with SFAS No. 86, "Accounting for the Cost of Computer Software to be Sold, Leased, or otherwise Marketed." Capitalization of software development costs begins upon the establishment of technological feasibility and is discontinued when the product is available for sale.

The establishment of technological feasibility and the ongoing assessment for recoverability of capitalized software development costs require considerable judgment by management with respect to certain external factors including, but not limited to, anticipated future gross revenues, estimated economic life, and changes in software and hardware technologies. Capitalized software development costs are comprised primarily of salaries and direct payroll-related costs and the purchase of existing software to be used in our software products.

Amortization of capitalized software development costs is provided on a product-by-product basis on the straight-line method over the estimated economic life of the products (not to exceed five years). Amortization of software development costs amounted to $381,390 and $334,509 for the nine months ended May 31, 2009 and May 31, 2008, respectively. We expect future amortization expense to vary due to increases in capitalized computer software development costs.

We test capitalized computer software costs for recoverability whenever events or changes in circumstances indicate that the carrying amount may not be recoverable within a reasonable time.

Property and Equipment
Property and equipment are recorded at cost, less accumulated depreciation and amortization. Depreciation and amortization are provided using the straight-line method over the estimated useful lives as follows:

Equipment	5 years
Computer equipment	3 to 7 years
Furniture and fixtures	5 to 7 years
Leasehold improvements	Shorter of life of asset or lease

Maintenance and minor replacements are charged to expense as incurred. Gains and losses on disposals are included in the results of operations.

Fair Value of Financial Instruments
For certain of our financial instruments, including cash and cash equivalents, accounts receivable, accounts payable, accrued payroll and other expenses, accrued bonuses to officers, and accrued warranty and service costs, the carrying amounts approximate fair value due to their short maturities.

Shipping and Handling
Shipping and handling costs, recorded as cost of sales, amounted to $75,058 and $78,986 for the nine months ended May 31, 2009 and May 31, 2008, respectively.

Research and Development Costs
Research and development costs are charged to expense as incurred until technological feasibility has been established. These costs consist primarily of salaries and direct payroll-related costs. It also includes purchased software which was developed by other companies and incorporated into, or used in the development of, our final products.

Income Taxes
The Company utilizes SFAS No. 109, "Accounting for Income Taxes," which requires the recognition of deferred tax assets and liabilities for expected future tax consequences of events that have been included in the financial statements or tax returns.

Under this method, deferred income taxes are recognized for the tax consequences in future years of differences between the tax bases of assets and liabilities and their financial reporting amounts at each year-end based on enacted tax laws and statutory tax rates applicable to the periods in which the differences are expected to affect taxable income. Valuation allowances are established, when necessary, to reduce deferred tax assets to the amount expected to be realized. The provision for income taxes represents the tax payable for the period and the change during the period in deferred tax assets and liabilities.

In June 2006, the Financial Accounting Standards Board (“FASB”) issued FASB interpretation No. 48, “Accounting for Uncertainty in Income Taxes – an Interpretation of FASB Statement No. 109” (“FIN 48”), which clarifies the accounting for uncertainty in income tax positions. The provisions of FIN 48 were effective for the Company on September 1, 2007.

At the end of fiscal year 2008, we recorded $424,000 in net deferred income tax liabilities. For the nine months ended May 31, 2009, we recorded a provision for income taxes in the amount of $650,846, resulting in a net deferred tax

liability of $489,100 at May 31, 2009. The evaluation of the deferred income tax assets is based on our history of generating taxable profits and our projections of future profits, as well as expected future tax rates. As of May 31, 2009, we have determined that it is more likely than not that the deferred tax assets will be realized. As such, no valuation allowance was recorded against the deferred tax assets. Significant judgment is required in these evaluations, and differences in future results from our estimates could result in material differences in the realization of these assets.

Customer relationships

The Company purchased customer relationships as a part of the acquisition of certain assets of Bioreason, Inc. in November 2005. Customer relationships was recorded at a cost of $128,042, and is being amortized over 78 months under the sum-of-the-years'-digits method. Amortization expense for the nine months ended May 31, 2009 and May 31, 2008 amounted to $15,335 and $19,823, respectively. Accumulated amortization as of May 31, 2009 and May 31, 2008 was $100,364 and $79,169, respectively.

Earnings per Share

The Company reports earnings per share in accordance with SFAS No. 128, "Earnings per Share." Basic earnings per share is computed by dividing income available to common shareholders by the weighted-average number of common shares available. Diluted earnings per share is computed similar to basic earnings per share except that the denominator is increased to include the number of additional common shares that would have been outstanding if the potential common shares had been issued and if the additional common shares were dilutive. The components of basic and diluted earnings per share for the nine months ended May 31, 2009 and May 31, 2008 were as follows:

	05/31/2009	05/31/2008
Numerator		
Net income attributable to common shareholders	$ 1,248,928	$ 1,560,731
Denominator		
Weighted-average number of common shares outstanding during the year	16,222,867	16,090,239
Dilutive effect of stock options	971,482	2,176,527
Common stock and common stock equivalents used for diluted earning per share	17,194,349	18,266,766

Stock-Based Compensation

Compensation costs related to stock options are determined in accordance with SFAS No. 123R using the modified prospective method. Under this method, compensation cost recognized during the nine months ended May 31, 2009 includes: (1) compensation cost for all share-based payments granted prior to, but not yet vested as of September 1, 2006, based on the grant date fair value estimated in accordance with the original provisions of SFAS No. 123 amortized over the options' vesting period, and (2) compensation cost for all share-based payments granted subsequent to September 1, 2006, based on the grant-date fair value estimated in accordance with the provisions of SFAS No. 123R, amortized on a straight-line basis over the options' vesting period. Stock-based compensation was $129,660 and $52,540 for the nine months ended May 31, 2009 and May 31, 2008, respectively, and is included in the condensed consolidated statements of operations as Selling, General and Administrative, and Research and Development expense.

Concentrations and Uncertainties

International sales accounted for 31% and 40% of net sales for the nine months ended May 31, 2009 and May 31, 2008, respectively. For Simulations Plus, Inc., two customers accounted for 28% of net sales during the nine months ended May 31, 2009, compared with two customers accounting for 24% of net sales during the nine months ended May 31, 2008. For Words+, Inc., two government agencies accounted for 33% of net sales during the nine months ended May 31, 2009, compared with one government agency accounting for 22% and one customer accounting for 15% of net sales during the nine months ended May 31, 2008.

The Company operates in the computer software industry, which is highly competitive and changes rapidly. The Company's operating results could be significantly affected by its ability to develop new products and find new distribution channels for new and existing products.

For Simulations Plus, two customers comprised 56% of its accounts receivable at May 31, 2009, of which 21% is from our distributor represents several Japanese companies, and three customers comprised 58% of accounts receivable at May 31, 2008, of which 22% is from our distributor representing several Japanese companies. For Words+, two government agencies comprised 40% of its accounts receivable at May 31, 2009, and one government agency comprised 35% of its accounts receivable at May 31, 2008.

The Company's subsidiary, Words+, Inc., purchases components for its main computer products from four manufacturers. Words+, Inc. also uses a number of pictographic symbols that are used in its software products which are licensed from a third party. The inability of the Company to obtain computers used in its products or to renew its licensing agreement to use pictographic symbols could negatively impact the Company's financial position, results of operations, and cash flows.

Recently Issued Accounting Pronouncements

On March 19, 2008, the Financial Accounting Standards Board (FASB) announced the issuance of Statement of Financial Accounting Standards No. 161, Disclosures about Derivative Instruments and Hedging Activities ("SFAS No. 161"). SFAS No. 161 amends Statement of Financial Accounting Standards No. 133, Accounting for Derivative Instruments and Hedging Activities ("SFAS No. 133") and was issued in response to concerns and criticisms about the lack of adequate disclosure of derivative instruments and hedging activities. SFAS No. 161 is focused on requiring enhanced disclosure on 1) how and why an entity uses derivative instruments and hedging activities; 2) how derivative instruments and related hedging activities are accounted for under SFAS No. 133; and 3) how derivative instruments and related hedging activities affect an entity's cash flows, financial position and performance.

To accomplish the three objectives listed above, SFAS No. 161 requires: 1) qualitative disclosures regarding the objectives and strategies for using derivative instruments and engaging in hedging activities in the context of an entity's overall risk exposure; 2) quantitative disclosures in tabular format of the fair values of derivative instruments and their gains and losses; and 3) disclosures about credit-risk related contingent features in derivative instruments.

SFAS No. 161 is effective for financial statements issued for fiscal years and interim periods beginning after November 15, 2008. Management believes the adoption of SFAS No. 161 for its financial assets and liabilities did not have a material impact on our consolidated financial statements.

In September 2006, the FASB issued SFAS No. 157, "Fair Value Measurements" ("SFAS 157"), which defines fair value, establishes a framework for measuring fair value and expands disclosures about fair value measurements. For financial assets and liabilities, SFAS 157 was effective for the Company in the first fiscal quarter of 2009. As permitted by FSP-FAS 157-2, SFAS 157 is effective for nonfinancial assets and liabilities for the Company during the first fiscal quarter of 2010. Management believes the adoption of SFAS 157 for its financial assets and liabilities did not have a material impact on the Company's consolidated financial statements and continues to evaluate the potential impact of the adoption of SFAS 157 related to its nonfinancial assets and liabilities.

In December 2007, the FASB issued SFAS No. 141 (revised 2007), "Business Combinations" ("SFAS 141R"), which amends SFAS 141. SFAS 141R establishes principles and requirements for how an acquirer recognizes and measures in its financial statements the identifiable assets acquired, the liabilities assumed, any resulting goodwill, and any noncontrolling interest in the acquiree. SFAS 141R also provides for disclosures to enable users of the financial statements to evaluate the nature and financial effects of the business combination. SFAS 141R will be effective for

the Company in the first fiscal quarter of 2010 and must be applied prospectively to business combinations completed on or after that date.

In December 2007, the FASB issued SFAS No. 160, "Noncontrolling Interests in Consolidated Financial Statements — an amendment of Accounting Research Bulletin No. 51" ("SFAS 160"), which establishes accounting and reporting standards for noncontrolling interests ("minority interests") in subsidiaries. SFAS 160 clarifies that a noncontrolling interest in a subsidiary should be accounted for as a component of equity separate from the parent's equity. SFAS 160 will be effective for the Company in the first fiscal quarter of 2010 and must be applied prospectively, except for the presentation and disclosure requirements, which will apply retrospectively. The Company is currently evaluating the potential impact that the adoption of SFAS 160 may have on its consolidated financial statements.

In May 2009, the FASB issued SFAS No. 165, "Subsequent Event" ("FAS 165"), which provides guidance to establish general standards of accounting for and disclosures of events that occur after the balance sheet date but before financial statements are issued or are available to be issued. FAS 165 also requires entities to disclose the date through which subsequent events were evaluated as well as the rational for why that date was selected. This disclosure should alert all users of financial statements that an entity has not evaluated subsequent events after that date in the set of financial statements being presented. FAS 165 is effective for interim and annual periods ending after June 15, 2009 and will be effective for the Company beginning with its annual period ending August 31, 2009. Since FAS 165 at most requires additional disclosures, the Company does not expect the adoption to have a material impact on its consolidated financial position, results of operations or cash flows.

In June 2009, the FASB approved the "FASB Accounting Standards Codification" (the "Codification") as the single source of authoritative nongovernmental U.S. GAAP to be launched on July 1, 2009. The Codification does not change current U.S. GAAP, but is intended to simplify user access to all authoritative U.S. GAAP by providing all the authoritative literature related to a particular topic in one place. All existing accounting standard documents will be superseded and all other accounting literature not included in the Codification will be considered nonauthoritative. The Codification is effective for interim and annual periods ending after September 15, 2009. The Codification is effective for the Company in the interim period ending November 30, 2009 and it does not expect the adoption to have a material impact on its consolidated financial position, results of operation or cash flows.

Note 3: PROPERTY AND EQUIPMENT

Property and equipment as of May 31, 2009 consisted of the following:

Equipment	$ 80,830
Computer equipment	366,897
Furniture and fixtures	61,498
Automobile	21,769
Leasehold improvements	53,898
Sub total	584,892
Less: Accumulated depreciation and amortization	(536,170)
Net Book Value	$ 48,722

Note 4: COMMITMENTS AND CONTINGENCIES

Employee Agreement
On August 9, 2007, the Company entered into an employment agreement with its President/Chief Executive Officer that expires in August 2009. The employment agreement provides for an annual salary of $250,000. At the CEO's request, this new agreement did not include an annual bonus, which had ranged up to $150,000 in all previous agreements. Thus, a savings to the Company of up to $75,000 per year has been realized as a result of this new agreement over the previous agreement. The agreement also provides that the Company may terminate the agreement upon 30 days' written notice if termination is without cause. The Company's only obligation would be to pay its President the greater of a) 12 months salary or b) the remainder of the term of the employment agreement from the date of notice of termination. The Compensation Committee of the Board of Directors is currently reviewing this agreement prior to its expiration on August 31 in order to determine terms for the next agreement to be effective September 1.

Litigation
The Company is not a party to any litigation at this time and is not aware of any pending litigation of any kind.

Note 5: SHAREHOLDERS' EQUITY

Stock Repurchase
Since December 2008, the Company has been buying back and canceling its own shares, and plans to continue its share repurchase in accordance with its share repurchase plan, which authorizes up to $2.5 million for the repurchase program through October 2009. The details of repurchases made during the nine months ended May 31, 2009 are listed in the following table:

Period	Total Number of Shares Purchased	Average Price Paid per Share	Remaining Funds Available Under the Share Repurchase Plan
12/01/08 to 12/31/08	90,632	$0.9764	$2,411,509
01/01/09 to 01/31/09	105,752	$1.0352	$2,302,032
02/01/09 to 02/28/09	73,118	$1.0086	$2,228,287
03/01/09 to 03/31/09	73,315	$0.9575	$2,158,086
04/01/09 to 04/30/09	55,580	$1.0045	$2,102,254
05/01/09 to 05/31/09	44,083	$1.1360	$2,052,175
	442,480	$1.0121	

As of 05/31/09

10

Stock Option Plan

In September 1996, the Board of Directors adopted, and the shareholders approved, the 1996 Stock Option Plan (the "Option Plan") under which a total of 250,000 shares of common stock had been reserved for issuance. In March 1999, the shareholders approved an increase in the number of shares that may be granted under the Option Plan to 500,000. In February 2000, the shareholders approved an increase in the number of shares that may be granted under the Option Plan to 1,000,000. In December 2000, the shareholders approved an increase in the number of shares that may be granted under the Option Plan to 1,250,000. Furthermore, in February 2005, the shareholders approved an additional 250,000 shares, resulting in the total number of shares that may be granted under the Option Plan to 1,500,000. All of the preceding numbers of options are based on numbers of options prior to the two-for-one stock split on August 14, 2006. The 1996 Stock Option Plan terminated in September 2006 by its term.

On February 23, 2007, the Board of Directors adopted and the shareholders approved the 2007 Stock Option Plan under which a total of 500,000 shares (1,000,000 shares after a 2-for-1stock split on October 1, 2007) of common stock had been reserved for issuance.

Options Outstanding & Exercisable at May 31, 2009

	Number of Options	Weighted-Average Exercise Price Per Share
Outstanding, August 31, 2008	2,714,536	$ 0.92
Granted	392,000	$ 1.09
Exercised	(169,000)	$ 0.54
Expired/Cancelled	(3,000)	$ 3.02
Outstanding, May 31, 2009	2,934,536	$ 0.96
Exercisable, May 31, 2009	2,230,136	$ 0.73

Options Outstanding & Unvested at May 31, 2009

	Number Outstanding	Weighted-Average Vesting Period (in years)	Weighted-Average Fair Market Price
Non-Vested, August 31, 2008.	414,000	2.65	$ 1.64
Granted	392,000		$ 0.77
Vested	(98,600)		$ 1.41
Cancelled	(3,000)		$ 2.27
Non-Vested, May 31, 2009	704,400	2.49	$ 1.18

The fair value of the options granted during the first nine months of fiscal year 2009 is estimated at $301,840. The fair value of these options was estimated at the date of grant using the Black-Scholes option-pricing model with the following weighted-average assumptions for the first nine months of fiscal year 2009: dividend yield of 0%, expected volatility of 69.78%, risk-free interest rate of 2.67%, and expected life of 7.68 years. The weighted-average fair values of options granted during the first nine months of fiscal year 2009 was $0.77, and the weighted-average exercise prices of options granted during the first nine months of fiscal year 2009 was $1.09. The total fair value of non-vested stock options as of May 31, 2009 was $831,192 and is amortizable over a weighted-average period of 2.49 years.

The Black-Scholes option valuation model was developed for use in estimating the fair value of traded options, which do not have vesting restrictions and are fully transferable. In addition, option valuation models require the input of highly subjective assumptions, including the expected stock price volatility. Because the Company's employee stock options have characteristics significantly different from those of traded options, and because changes in the subjective input assumptions can materially affect the fair value estimate, in management's opinion, the existing models do not necessarily provide a reliable single measure of the fair value of its employee stock options.

The weighted-average remaining contractual life of options outstanding issued under the Plan was 4.1 years at May 31, 2009. The exercise prices for the options outstanding at May 31, 2009 ranged from $0.26 to $3.03, and the information relating to these options is as follows:

Exercise Price		Awards Outstanding			Awards Exercisable		
Low	High	Quantity	Weighted-Average Remaining Contractual Life	Weighted-Average Exercise Price	Quantity	Weighted-Average Remaining Contractual Life	Weighted-Average Exercise Price
$0.26	$0.50	836,936	1.6 years	$ 0.37	836,936	1.6 years	$ 0.37
$0.51	$0.75	795,500	0.7 years	$ 0.66	795,500	0.7 years	$ 0.66
$0.76	$1.25	969,100	7.4 years	$ 1.06	541,100	6.0 years	$ 1.14
$1.26	$3.03	333,000	8.8 years	$ 2.83	56,600	8.7 years	$ 3.03
		2,934,536	4.1 years	$ 0.96	2,230,136	2.5 years	$ 0.73

Other Stock Options

As of May 31, 2009, the independent members of the Board of Directors hold options to purchase 63,824 shares of common stock at exercise prices ranging from $0.30 to $6.68.

	Number of Options	Weighted-average exercise price
Options Outstanding	63,824	$ 1.59
Options Exercisable	45,624	$ 1.04

Note 6: SEGMENT AND GEOGRAPHIC REPORTING

We account for segments and geographic revenues in accordance with SFAS No. 131, “Disclosure about Segments of an Enterprise and Related Information.” Our reportable segments are strategic business units that offer different products and services. Results for each segment and consolidated results are as follows for the nine months ended May 31, 2009 and May 31, 2008 (in thousands):

May 31, 2009

	Simulations Plus, Inc	Words +, Inc.	Eliminations	Total
Net Sales	$ 5,194	$ 2,110		$ 7,304
Income (loss) from operations	1,326	(77)		1,249
Identifiable assets	12,417	2,045	$ (1,687)	12,775
Capital expenditures	15	20		35
Depreciation and Amortization	374	39		413

May 31, 2008

	Simulations Plus, Inc	Words +, Inc.	Eliminations	Total
Net Sales	$ 4,963	$ 2,169		$ 7,132
Income (loss) from operations	2,054	108		2,162
Identifiable assets	10,825	2,212	$ (1,683)	11,354
Capital expenditures	-	68		68
Depreciation and Amortization	13	27		40

In addition, the Company allocates revenues to geographic areas based on the locations of its customers. Geographical revenues for the nine months ended May 31, 2009 and May 31, 2008 were as follows (in thousands):

May 31, 2009

	North America	Europe	Asia	Oceania	South America	Total
Simulations Plus, Inc.	3,023	1,457	714	-	-	$ 5,194
Words+, Inc.	2,027	24	17	42	-	2,110
Total	5,050	1,481	731	42	-	7,304

May 31, 2008

	North America	Europe	Asia	Oceania	South America	Total
Simulations Plus, Inc.	2,527	1,632	804	-	-	4,963
Words+, Inc.	1,778	336	22	31	2	2,169
Total	4,305	1,968	826	31	2	7,132

Note 7: EMPLOYEE BENEFIT PLAN

We maintain a 401(K) Plan for all eligible employees. We make matching contributions equal to 100% of the employee's elective deferral, not to exceed 4% of total employee compensation. We can also elect to make a profit-sharing contribution. Contributions by the Company to this Plan amounted to $60,661 and $53,059 for the nine

months ended May 31, 2009 and May 31, 2008, respectively.

Board of Directors approved that Bonus and Commissions to be excluded for the Company matching effective as of January 1, 2009.

Note 8: INVESTMENT

On January 2, 2009, the Company received a confirmation from UBS Financial Services, Inc. that all Auction Rated Securities (ARS) were sold and payment was settled on January 5, 2009. As a result, the par value of $750,000 plus accrued interest of $301 became available to the Company as cash on January 5, 2009. The ARSs were presented as an investment at August 31, 2008.

Note 9: SUBSEQUENT EVENT

Since December 2008, the Company has been buying back its own shares, and plans to continue its share repurchase in accordance with its share repurchase plan, which authorizes up to $2.5 million for the repurchase program through October 2009. The details of repurchases made since May 31, 2009 are listed in the following table. Thus, adding these shares to those described above through May 31, the total number of shares repurchased through July 10, 2009 was 648,135.

Period	Total Number of Shares Purchased	Average Price Paid per Share	Remaining Funds Available Under the Share Repurchase Plan
06/01/2009 to 06/30/2009	171,740 *	$1.3885	$1,813,724
07/01/2009 through 07/10/2009	33,915	$1.5721	$1,760,406
Total	205,655	$1.4188	

* Includes repurchase of 50,000 shares at $1.24 on June 5, 2009 from Walter Woltosz, CEO of the Company.

From June 1, 2009 to July 10, 2009, an additional 34,824 stock options to purchase shares have been exercised by employees and board of directors that generated $13,621 in cash.

Item 2. Management's Discussion and Analysis or Plan of Operations

Forward-Looking Statements

Certain statements in this Quarterly Report on Form 10-Q, or the "Report," are "forward-looking statements." These forward-looking statements include, but are not limited to, statements about the plans, objectives, expectations and intentions of Simulations Plus, Inc., a California corporation (referred to in this Report as the "Company") and other statements contained in this Report that are not historical facts. Forward-looking statements in this Report or hereafter included in other publicly available documents filed with the Securities and Exchange Commission, or the "Commission," reports to our stockholders and other publicly available statements issued or released by us involve known and unknown risks, uncertainties and other factors which could cause our actual results, performance (financial or operating) or achievements to differ from the future results, performance (financial or operating) or achievements expressed or implied by such forward-looking statements. Such future results are based upon management's best estimates based upon current conditions and the most recent results of operations. When used in this Report, the words "expect," "anticipate," "intend," "plan," "believe," "seek," "estimate" and similar expressions are generally intended to identify forward-looking statements, because these forward-looking statements involve risks and uncertainties. There are important factors that could cause actual results to differ materially from those expressed or implied by these forward-looking statements, including our plans, objectives, expectations and intentions and other factors.

General

BUSINESS

Simulations Plus, Inc. (the “Company” or “Simulations Plus”, or "we" or "our") and its wholly owned subsidiary, Words+, Inc. (“Words+”) produce different types of products: (1) Simulations Plus, incorporated in 1996, develops and produces software for use in pharmaceutical research and for education, and also provides contract research services to the pharmaceutical industry, and (2) Words+, founded in 1981, produces computer software and specialized hardware for use by persons with disabilities. For the purposes of this document, we sometimes refer to the two businesses as “Simulations Plus” when referring to the business that is primarily pharmaceutical software and services, and “Words+” when referring to the business that is primarily assistive technologies for persons with disabilities.

SIMULATIONS PLUS

PRODUCTS
We currently offer four software products for pharmaceutical research: ADMET Predictor™, ClassPharmer™, DDDPlus™, and GastroPlus™.

ADMET Predictor
Every drug molecule that fails in clinical trials, and every approved drug that gets withdrawn from the market, was bad from the time it was first drawn by a chemist or generated by a computer. They don’t become bad later. Thus, the ability to predict unsuitable characteristics of new molecules offers the promise of avoiding costly programs that end up in late-stage failures. Although not every failure mode can be predicted in this manner, those that can provide a means to reduce the number of failures that occur after years of work and millions of dollars have been spent.

ADMET (Absorption, Distribution, Metabolism, Excretion and Toxicity) Predictor consists of a library of statistically significant numerical models that predict various properties of chemical compounds from just their molecular structures. Our models are built using a machine learning approach that is based primarily on artificial neural network ensembles (groups of artificial neural networks) that has been demonstrated to provide the most accurate prediction capabilities in any commercially available software today.

This capability means a chemist can merely draw a molecule diagram and get estimates of these properties, even though the molecule has never existed. Drug companies continually search through millions of such "virtual" molecular structures as they attempt to find new drugs. It has been estimated that there are somewhere on the order of 1062 possible drug-like molecular structures. That is such a huge number that it is difficult to comprehend. If we could evaluate a billion molecules (109) per second, it would take 1053 seconds to evaluate them all -- that's about 1045 years. The age of the universe is said to be less than 1010 years. Clearly, we will never be able to make and test evaluate all of them, so computerized methods are the only hope to even scratch the surface of the total "chemical space" for potential pharmaceutical products.

The vast majority of drug-like molecules are not suitable as medicines for various reasons. Some have such low solubility that they will not dissolve well, some have such low permeability through the intestinal wall that they will not be absorbed well as an oral dose (about 80% of medications), some degrade so quickly that they are not stable enough to have a useful shelf life, some bind to proteins (like albumin) in blood to such a high extent that little unbound drug is available to reach the target, and many will be toxic in various ways. Identification of such properties in the computer enables researchers to eliminate poor compounds without spending time and money to make them and run experiments to identify their weaknesses. Today, many molecules can be eliminated on the basis of computer predictions provided by ADMET Predictor.

Several independent studies have been published that compare the accuracy of software programs like ADMET Predictor. In each case, ADMET Predictor has been ranked first in accuracy (it was ranked second in one study, but that study was later redone with a more difficult set of test compounds and a newer version of ADMET Predictor, and it was then ranked first). Not one other software product was consistently in the top 4 in these studies. This is a remarkable accomplishment, considering the greater size and resources of many of our competitors.

ADMET Predictor includes ADMET Modeler™. ADMET Modeler was first released in July of 2003 as a separate product, and was integrated into ADMET Predictor in 2006. This powerful program automates the training of the predictive models used in ADMET Predictor, so they are produced in a small fraction of the time once required. For example, new toxicity models were developed in a matter of a few hours once we completed the tedious effort of "cleaning up" the databases (which often contain a significant number of errors). Prior to the availability of ADMET Modeler, we would have needed as much as three months for each new model after cleaning the databases to obtain similar results.

Pharmaceutical companies spend enormous amounts of money conducting a wide variety of experiments on new molecules each year. Using such data to build predictive models provides a second return on this investment; however, in the past, model-building has traditionally been a tedious activity performed by specialists. With ADMET Modeler integrated into ADMET Predictor, scientists without model-building experience can now use their own experimental data to quickly create high-quality predictive models.

During this reporting period, improvement of ADMET Predictor/Modeler has continued. Under a funded collaboration with Pfizer, we added the capability for scientists to run large molecular libraries through ADMET Predictor to generate the predicted dose amount that would be required to achieve an effective concentration level for each potential new drug. This capability requires the integration of the customer's experimental data with predictions when no experiments have been run, so that the effects of a wide variety of properties that interact to result in a plasma concentration can be predicted. This is accomplished by the integration of a small GastroPlus engine within ADMET Predictor that runs the simulations needed to estimate plasma concentrations.

We expect to release the next version in late July 2009. This new version will also include a new set of toxicity predictions, expanding the program's capabilities into this important, and almost unlimited area (because there are so many kinds of toxicities). Every new predicted property that can be used to help triage bad compounds early in discovery has the potential to save large amounts of time and money.

ADMET Predictor is compatible with the popular Pipeline Pilot™ software offered by SciTegic, a subsidiary of Accelrys. This software serves as a tool to allow chemists to run several different software programs in series to accomplish a set workflow for large numbers of molecules. In early discovery, chemists often work with hundreds of thousands or millions of "virtual" molecules – molecules that exist only in a computer. The chemist tries to decide which few molecules from these large "libraries" should be made and tested. Using Pipeline Pilot with ADMET Predictor (and ClassPharmer – see below), perhaps in conjunction with other software products, the chemist can create and screen very large libraries faster and more efficiently than running each program by itself.

In August 2008, we had resubmitted a Phase II NIH SBIR (Small Business Innovation Research) grant proposal. After the end of this reporting period, we were advised that this grant will be funded at a level of $375,000. We have continued this work under our own funding, and we've demonstrated further improvements in predictive capability, which we are incorporating into the next release of ADMET Predictor.

ClassPharmer

ClassPharmer continues to evolve into an ever more powerful tool for medicinal and computational chemists. Coupled with ADMET Predictor, the two programs provide an unmatched capability for chemists to search through huge libraries of compounds to find the most interesting classes and molecules that are active against a particular target. In addition, ClassPharmer with ADMET Predictor can take an interesting molecule and generate high quality analogs (i.e., similar new molecules) using several different algorithms to ensure that the new molecules are both active against the target while also being acceptable in a variety of ADMET (Absorption, Distribution, Metabolism, Excretion and Toxicity) properties.

Improvements during the third quarter were focused on incorporating more new features requested by our users around the world, as well as adding other new capabilities identified in-house. We released ClassPharmer 4.6 in January 2009, and we expect another release in the near future with a new "scaffold hopping" feature. This feature enables chemists to substitute the core (scaffold) portion of a molecule while retaining other atoms around the periphery. In previous versions, ClassPharmer had only the inverse capability – to replace the atoms surrounding the core. Scaffold hopping has been a technique with growing interest among chemists, and we expect that added to ClassPharmer already best-in-class performance, this new capability will attract additional ClassPharmer users.

ClassPharmer's molecule design capabilities provide ways for chemists to rapidly generate large numbers of novel chemical structures based on intelligence from compounds that have already been synthesized and tested, or from basic chemical reactions selected by the user. Export of results is available in Microsoft Excel™ format as well as other convenient file formats requested by users.

DDDPlus

DDDPlus sales have continued to grow as formulation scientists continue to recognize the value of this one-of–a–kind simulation software in their work. Improvements have been added to further enhance the value of this product, including numerous user convenience features have been added, as well as more sophisticated handling of dosage forms that incorporate multiple polymers for controlled release. Work on the next update of DDDPlus has included making the program match the user interface in our flagship GastroPlus product as closely as possible since many formulation scientists can use both programs. Additions to the programs capabilities and built-in databases for excipient ingredients and dissolution media have also been made. A major new release of DDDPlus was released in late April 2009.

GastroPlus

GastroPlus continues to enjoy its "gold standard" status in the industry for its class of simulation software. It is used from early drug discovery through preclinical development and into early clinical trials. At an international conference in Shanghai, China, in May 2008, Pfizer scientists presented a scientific poster describing a two-year study in which all four commercially available PBPK (physiologically based pharmacokinetics) simulation programs on the market were compared for their ability to predict human pharmacokinetics from preclinical (animal and in vitro) data. The study was divided into two arms: intravenous and oral dosing. GastroPlus was ranked first in both arms. No other software was ranked consistently second or third. This independent evaluation, which was accomplished via analysis of 21 Pfizer proprietary compounds with data from early discovery all the way through human trials, provides the strongest possible validation of the superiority of GastroPlus in pharmaceutical research and development.

The information provided through GastroPlus simulations guides project decisions in various ways. Among the kinds of knowledge gained through such simulations are: (1) the best "first dose in human" for a new drug prior to Phase I trials, (2) whether a potential new drug compound is likely to be absorbed at high enough levels to achieve the desired blood concentrations needed for effective therapy, (3) whether the absorption process is affected by certain enzymes and transporter proteins in the intestinal tract that may cause the amount of drug reaching the blood to be very different from one region of the intestine to another, (4) when certain properties of a new compound are probably adequately estimated through computer ("in silico") predictions or simple experiments rather than through more expensive and time-consuming in vitro or animal experiments, (5) what the likely variations in blood and tissue concentration levels of a new drug would be in a large population, in different age groups or in different ethnic groups, and (6) whether a new formulation for an existing approved drug is likely to demonstrate "bioequivalence" (equivalent blood concentration versus time) to the currently marketed dosage form in a human trial.

In May 2008 we announced the current release of GastroPlus (version 6.0) – a major new release that includes several important improvements to the program. We improved the PKPlus™ Module to enable it to fit pharmacokinetic models to multiple data sets, including both intravenous and oral dosage forms. The feedback we have received from customers for that change has been enthusiastic. We made further improvements to the new sophisticated kidney model to simulate how drugs are cleared in urine. We added numerous convenience features requested by our users. We also added the ability of the program to track metabolites of a parent drug, including metabolites of metabolites, to as many levels as desired. This is a significant new capability because it allows the user to predict how much of each metabolite will be generated, and into which tissues the metabolite is likely to partition. Some metabolites can be therapeutically active, while others can be toxic, so knowing how much is produced and where it goes is valuable information to assess the likelihood of both therapeutic and adverse effects.

18

Since last May, the improvements to GastroPlus have been many and complex. Most of these developments were funded through our funded collaborations with three of the top five pharmaceutical companies in the world. We are adding ocular delivery of drugs under one collaboration, pulmonary delivery under another, and drug-drug interaction analysis under a third. These capabilities will further extend the commanding lead GastroPlus enjoys in the marketplace.

Our marketing intelligence and reorder history indicate that GastroPlus continues to dominate its market niche in the number of users worldwide. In addition to virtually every major pharmaceutical company, licenses include government agencies in the U.S and abroad, a growing number of smaller pharmaceutical and biotech companies, generic drug companies, and drug delivery companies (companies that design the tablet or capsule for a drug compound that was developed by another company). Although these companies are smaller than the pharmaceutical giants, they can also save considerable time and money through simulation. We believe this part of the industry, which includes many hundreds of companies, represents major growth potential for GastroPlus. Our experience has been that the number of new companies adopting GastroPlus has been growing steadily, adding to the base of annual licenses each year.

CONTRACT RESEARCH AND CONSULTING SERVICES

Our recognized world-class expertise in oral absorption and pharmacokinetics is evidenced by the fact that our staff members have been speakers or presenters at over 50 prestigious scientific meetings worldwide in the past five years. We frequently conduct contracted studies for customers who prefer to have studies run by our scientists rather than to license our software and train someone to use it. The demand for our consulting services has been increasing steadily, and we expect this trend to continue. Long-term collaborations and shorter-term consulting contracts serve both to showcase our technologies and as a way to build and strengthen customer relationships.

WORDS+ SUBSIDIARY

PRODUCTS

Our wholly owned subsidiary, Words+, Inc., has been an industry pioneer and technology leader for over 27 years in introducing and improving augmentative and alternative communication and computer access software and devices for disabled persons. We intend to continue to be at the forefront of the development of new products. We will continue to enhance our major software products, E Z Keys™ and Say-it! SAM™, as well as our line of hardware products. We are also considering acquisitions of other products, businesses and companies that are complementary to our existing augmentative and alternative communication and computer access business lines. We acquired the Say-it! SAM technologies from SAM Communications, LLC of San Diego in December 2003. This acquisition gave us our smallest, lightest augmentative communication system, which is based on a Hewlett-Packard iPAQ personal digital assistant (PDA). PDA-based communication devices have been very successful in the augmentative communication market, and this technology purchase enabled us to move into this market segment faster and at lower cost than developing the product ourselves. SAM-based products now account for a significant share of Words+ revenues. Since the acquisition of the Say-it! SAM technologies, we have continued to add new functionality to the SAM software and to offer it on additional hardware platforms.

During last fiscal year, after the introduction of the newest Say-it! SAM version late in the first quarter, sales of our new PDA-based (personal-digital-assistant-based) Say-it! SAM augmentative communication device set new records, contributing nicely to the highest quarter in our history in the third quarter. Just before the end of the last quarter we introduced the Conversa™. This product offers the most human-sounding synthetic speech output available in the marketplace utilizing AT&T synthetic voices and our new custom designed Sound Pack. To quote one young adult client who changed to the Conversa after using a variety of augmentative communication devices from our competitors for most of her life "I actually sound like a regular woman for the first time in my life!" We are adding the Sound Pack design to other products.

We have clients utilizing new access methods such as the Fiber Optic Switch that is a new part of our product line, a new EMG (muscle signal) switch called Libertas and eye gaze systems from a variety of manufacturers, and we are regularly evaluating and interfacing new access technology.

Results of Operations

Comparison of Three Months Ended May 31, 2009 and May 31, 2008.

The following table sets forth our consolidated statements of operations (in thousands) and the percentages that such items bear to net sales:

	Three Months Ended			
	05/31/09		05/31/08	
Net sales	$ 2,713	100%	$ 2,968	100%
Cost of sales	543	20.0	624	21.0
Gross profit	2,170	80.0	2,344	79.0
Selling, general and administrative	989	36.5	942	31.7
Research and development	334	12.3	222	7.5
Total operating expenses	1,323	48.8	1,164	39.2
Income from operations	847	31.2	1,180	39.8
Other income	41	1.5	8	0.3
Net income before taxes	888	32.7	1,188	40.0
(Provision for) income taxes	(319)	(11.8)	(435)	(14.7)
Net income	$ 569	20.9%	$ 753	25.4%

Net Sales

Consolidated net sales decreased $255,000, or 8.6%, to $2,713,000 in the third fiscal quarter of 2009 (3QFY09) from $2,968,000 in the third fiscal quarter of 2008 (3QFY08). Our sales from pharmaceutical and educational software increased approximately $10,000, or 0.5%; and our Words+, Inc. subsidiary's sales decreased approximately $265,000, or 26.7%, for the quarter. We attribute the increase in pharmaceutical software sales primarily to new software licensing, new customers, and sale of new modules to existing customers as well as increases in the number of licenses with existing customers, and our funded collaborations with large pharmaceutical companies that outweighed the loss of a few small customers and a decline in renewal license revenues of approximately $124,000 that resulted in an order from one large pharmaceutical company that was received late, and so was unlocked and its revenue recognized in the 4th fiscal quarter vs. the 3rd quarter.

We attribute the decrease in Words+ sales primarily to a decrease in "Freedom" products with "EZKeys" or "Say-it! SAM" software, which are based on Windows XP systems, and accessories to go with those products. Another factor is due to decline in revenue from Say-it! SAM" handheld speech output devices. In 3QFY08, we had significant revenues from our "Say-it! SAM" speech output device kits without PDA hardware for an overseas wholesaler; however we did not have such an order in 3QFY09.

Cost of Sales

Consolidated cost of sales decreased $81,000, or 12.9%, to $543,000 in 3QFY09 from $624,000 in 3QFY08. Cost of sales as a percentage of revenue for 3QFY09 slightly decreased by 1.0% to 20.0% from 21.0% in 3QFY08. For Simulations Plus, cost of sales increased $25,000, or 11.8%. As a percentage of revenue, cost of sales also increased to 12.0% in 3QFY09 from 10.8% in 3QFY08. A significant portion of cost of sales for pharmaceutical software products is the systematic amortization of capitalized software development costs, which is an independent fixed cost rather than a variable cost related to sales. This amortization cost increased approximately $31,000, or 35.8%, in 3QFY09 compared with 3QFY08. Royalty expense, which is a variable cost, relates to sales of our GastroPlus core program as well as our new ADMET Predictor Enslein Metabolism module, decreased approximately $6,000, or 4.5%, in 3QFY09 compared with 3QFY08 due to decreases in sales from those products.

For Words+, cost of sales decreased $106,000, or 25.8%. As a percentage of revenue, cost of sales were very identical, 41.8% in 3QFY09 from 41.3% in 3QFY08.

Gross Profit

Consolidated gross profit decreased $174,000, or 7.4%, to $2,170,000 in 3QFY09 from $2,344,000 in 3QFY08. We attribute this decrease to an increase in sales of pharmaceutical software was not large enough to cover an increase in cost of goods sold in addition to a decrease in gross profit from Words+ products.

Selling, General and Administrative Expenses

Consolidated selling, general and administrative (SG&A) expenses increased $47,000, or 5.0%, to $989,000 in 3QFY09 from $942,000 in 3QFY08. For Simulations Plus, SG&A increased $73,000, or 13.1%. As a percentage of sales, SG&A also increased to approximately 31.9% in 3QFY09 from approximately 28.4% in 3QFY08. The major increases in SG&A expenses were expanded trade show expenses, travel expenses, and consultant fees which outweighed decreases in commissions and professional fees.

For Words+, SG&A expenses decreased $26,000, or 6.9%, due primarily to decreases in commissions, depreciation, repairs, and contributions. These decreases outweighed increases in bad debts, depreciation, and salaries which are results of a consultant becoming an employee and 2 additional sales employees.

Research and Development

We incurred approximately $472,000 of consolidated research and development costs during 3QFY09. Of this amount, $138,000 was capitalized and $334,000 was expensed. In 3QFY08, we incurred $428,000 of consolidated research and development costs, of which $206,000 was capitalized and $222,000 was expensed. The increase of $44,000, or 10.3%, in total research and development expenditures from 3QFY08 to 3QFY09 was due primarily to salaries of new hires and salary increases to existing staff.

Other income (expense)
Net other income (expense) in 3QFY09 increased by $33,000, or 437.02%, to $41,000 in 3QFY09 from $8,000 in 3QFY08. This is due primarily to an unrecognized loss incurred in Auction Rate Securities (ARS) held in 3QFY08 with UBS Financial Services Inc. Those ARSs were redeemed at full face value plus interest in early 2009 so the loss never materialized.

Provision for Income Taxes
Our provision for income taxes decreased by $116,000, or 26.7%, to $319,000 in 3QFY09 from $435,000. As a percentage of net income, the tax is increased from 36.6% in 3QFY08 to 35.9% in 3QFY09 due primarily to our estimation of higher provision for income tax in fiscal year 2009.

Net Income
Consolidated net income decreased by $184,000, or 24.4%, to $569,000 in 3QFY09 from $753,000 in 3QFY08. We attribute this decrease in profit primarily to the increases in operating expenses, tax provision and a decrease in gross profit.

Comparison of Nine Months Ended May 31, 2009 and May 31, 2008.

The following table sets forth our consolidated statements of operations (in thousands) and the percentages that such items bear to net sales:

	Nine Months Ended			
	05/31/09		05/31/08	
Net sales	$ 7,303	100%	$ 7,132	100%
Cost of sales	1,622	22.2	1,565	21.9
Gross profit	5,681	77.8	5,567	78.1
Selling, general and administrative	2,929	40.1	2,705	37.9
Research and development	996	13.6	700	9.8
Total operating expenses	3,925	53.7	3,405	47.7
Income from operations	1,756	24.0	2,162	30.3
Other income	144	2.0	133	1.9
Net income before taxes	1,900	26.0	2,295	32.2
(Provision for) income taxes	(651)	(8.9)	(735)	(10.3)
Net income	$ 1,249	17.1%	$ 1,561	21.9%

Net Sales
Consolidated net sales increased $171,000, or 2.4%, to $7,303,000 in the first nine months of fiscal year 2009 (FY09) from $7,132,000 in the first nine months of fiscal year 2008 (FY08). Our sales from pharmaceutical software and services increased approximately $231,000, or 4.7%, however, our Words+, Inc. subsidiary's sales decreased approximately $60,000, or 2.7%, for the first nine months of fiscal year 2009.

We attribute the increase in pharmaceutical software sales primarily to increased licenses, both to new customers and for new modules, additional licenses to renewal customers, funded collaborations, and contract studies.

We attribute the decrease in Words+ sales primarily to decrease in sales of "TuffTalker" and "MessageMate", mounting systems, and "Freedom" products with EZKeys software which are based on Windows XP systems. Those decreases outweighed an increase in revenue from our new "Conversa™" with Say-it! SAM software.

22

Cost of Sales

Consolidated cost of sales increased $57,000, or 3.7%, to $1,622,000 in FY09 from $1,565,000 in FY08. Cost of sales as a percentage of revenue for the first nine months of FY09 and FY08 were almost identical with a small increase of 0.3%. For Simulations Plus, cost of sales increased $55,000, or 8.9%. As a percentage of revenue, cost of sales increased slightly from 12.5% in FY08 to 13.0% in FY09. A significant portion of cost of sales for pharmaceutical software products is the systematic amortization of capitalized software development costs, which is an independent fixed cost rather than a variable cost related to sales. This amortization cost increased approximately $44,000, or 14.4%, in FY09 compared with FY08. Royalty expense increased approximately $11,000, or 3.6%, in FY09 compared with FY08.

For Words+, cost of sales increased $2,000, or 0.2%. As a percentage of revenue, cost of sales was almost identical, with a small increase of 1.3% between FY09 and FY08. We attribute the small percentage increase in cost of sales for Words+ primarily to sales from products with high-cost tablets systems. Those costs were offset by a decrease in production wages, and royalty costs which is also a part of cost of sales, resulting in a smaller percentage increase.

Gross Profit

Consolidated gross profit increased $114,000, or 2.1%, to $5,681,000 in FY09 from $5,567,000 in FY08. We attribute this increase to increased sales of pharmaceutical software and services which outweighed a decrease in gross profit from Words+ products.

Selling, General and Administrative Expenses

Consolidated selling, general and administrative (SG&A) expenses increased $225,000, or 8.3%, to $2,929,000 in FY09 from $2,705,000 in FY08. For Simulations Plus, SG&A increased $121,000, or 7.3%. As a percentage of sales, SG&A slightly increased 0.9%, from 33.3% in FY08 to 34.2% in FY09. The major increases in SG&A expenses were expanded trade shows due to our more aggressive marketing and sales campaign this year, travel, consulting fees, salaries, and 401k expenses, which outweighed decreases in commissions and investor relations (namely a payment to AMEX for a stock split).

For Words+, SG&A expenses increased $104,000, or 9.9%. As a percentage of sales, SG&A increased 6.3%, from 48.4% in FY08 to 54.7% in FY09. We attribute this increase in SG&A primarily to an increase in write-off of potential bad debts and salary expenses by hiring sales employees which outweighed a decrease in contract labor and depreciation expense.

Research and Development

We incurred approximately $1,487,000 of research and development costs for both companies during the first nine months of FY09. Of this amount, $491,000 was capitalized and $996,000 was expensed. In the first nine months of FY08, we incurred $1,295,000 of research and development costs, of which $595,000 was capitalized and $700,000 was expensed. The increase of $192,000, or 14.8%, in total research and development expenditures from the first nine months of FY08 to the first nine months of FY09 was due to a combination of salaries for new hires and salary increases and bonuses to existing staff.

Other income

Net other income in the first nine months of FY09 increased by $11,000, or 8.0%, from $133,000 to $144,000. This is due primarily to an unrecognized loss incurred in Auction Rate Securities (ARS) held in 3QFY08 with UBS Financial Services Inc. Those ARSs were redeemed at full face value plus interest in early 2009, so the loss never materialized. This reduction in unrecognized loss was offset by decreased interest revenues from Money Market accounts.

Provision for Income Taxes

The provision for income taxes decreased by $84,000, or 11.4%, to $651,000 in the first nine months of FY09 from $735,000 in the first nine months of FY08. As a percentage of net income, the tax rate increased from 32.0% in the nine months of FY08 to 34.3% in the nine months of FY09. This increase is due primarily to our estimation of higher provision for income tax in fiscal year 2009. The tax rate used in this report is still lower than standard rate because of current R&D tax credits generated and used during this reporting period.

Net Income (loss)

Consolidated net income decreased by $312,000, or 20.0%, to $1,249,000 in the first nine months of FY09 from $1,561,000 in the first nine months of FY08. We attribute this decrease in profit primarily to increases in operating expenses, the increased provision rate for income taxes which outweighed increases in gross profit.

Liquidity and Capital Resources

Our principal sources of capital have been cash flows from our operations. We have achieved continuous positive operating cash flow over the last six fiscal years. We believe that our existing capital and anticipated funds from operations will be sufficient to meet our anticipated cash needs for working capital and capital expenditures for the foreseeable future. Thereafter, if cash generated from operations is insufficient to satisfy our capital requirements, we may open a revolving line of credit with a bank, or we may have to sell additional equity or debt securities or obtain expanded credit facilities. In the event such financing is needed in the future, there can be no assurance that such financing will be available to us, or, if available, that it will be in amounts and on terms acceptable to us. If cash flows from operations became insufficient to continue operations at the current level, and if no additional financing was obtained, then management would restructure the Company in a way to preserve its pharmaceutical and disability businesses while maintaining expenses within operating cash flows. In January 2009, the $750,000 investment in Auction Rate Securities was repurchased by UBS Financial Services, Inc. at par value plus interest.

Item 3. Quantitative and Qualitative Disclosures about Market Risk

Our risk from exposure to financial markets is limited to foreign exchange variances and fluctuations in interest rates. We may be subject to some foreign exchange risks. Most of our business transactions are in U.S. dollars, although we generate significant revenues from customers overseas. The exception is that we were compensated in Japanese yen by some Japanese customers and one European customer. As a result, we experienced a small gain from currency exchange in the first nine months of FY09. In the future, if foreign currency transactions increase significantly, then we may mitigate this effect through foreign currency forward contracts whose market-to-market gains or losses are recorded in "Other Income or expense" at the time of the transaction. To date, exchange rate exposure has not resulted in a material impact.

Item 4. Controls and Procedures

(a) Evaluation of disclosure controls and procedures.

(b) Changes in internal controls over financial reporting.

There were no changes in the Company's internal controls over financial reporting during the Company's most recent fiscal quarter that have materially affected, or are reasonably likely to materially affect, the Company's internal controls over financial reporting.

Part II. Other Information

Item 1. Legal Proceedings
The Company is not a party to any legal proceedings and is not aware of any pending legal proceedings of any kind.

Item 2. Changes in Securities
Since December 2008, the Company has been buying back its own shares, and plans to continue its share repurchase in accordance with its share repurchase plan, which authorizes up to $2.5 million for the repurchase program through October 2009. As a result, the Company has bought back 442,480 shares by the end of May 31, 2009.

Item 3. Defaults Upon Senior Securities
None.

Item 4. Submission of Matters to a Vote of Security Holders
None.

Item 5. Other Information
None

Item 6. Exhibits and Reports on form 8-K

(a) Exhibits:
31.1 - 2 Certification of Chief Executive Officer and Chief Financial Officer
32 Certification pursuant to Sec. 906 of the Sarbanes-Oxley Act of 2002

SIGNATURE

In accordance with Section 13 or 15 (d) of the Securities Exchange Act of 1934, the Registrant caused this report to be signed on its behalf by the undersigned, thereunto duly authorized, in the City of Lancaster, State of California, on July 15, 2009.

Simulations Plus, Inc.

Date: July 15, 2009 By: /s/ MOMOKO BERAN
Momoko Beran
Chief Financial Officer